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In the Courts

*By Michael R. O'Donnell and James V. Mazewski**

Nevada Court Issues Significant Guidance on the Interpretation of ALTA HOA Endorsements

The Supreme Court of Nevada (the Court) has issued an important decision in the matter of *Deutsche Bank National Trust Company v. Fidelity National Title Insurance Company*,[1] providing guidance on the interpretation and application of American Land Title Association (ALTA) and California Land Title Association (CLTA) endorsements 100(1)(a), 100(2)(a), and 115.2(2).

BACKGROUND

In May 2004, James and Sharon Lutkin (the Lutkins) purchased real property in Mira Vista, Nevada (the Property), obtaining a mortgage from New Century Mortgage Corporation (New Century) as part of the purchase, with Fidelity National Title Insurance Company (Fidelity) issuing New Century a title-insurance policy covering both New Century and any of its subsequent assigns (the Policy).

After the Lutkins' purchase was complete, New Century assigned Deutsche Bank National Trust Company (Deutsche Bank) a Deed of Trust to the Property. The Property was part of a Homeowners Association (the HOA), and in 2011, the Lutkins failed to pay an assessment they owed to the HOA. In August 2012, the HOA successfully foreclosed on the Property, took title, and sold the Property to G&P Investment Enterprises, LLC (G&P), with G&P in turn selling the Property to TRP Fund VI, LLC (TRP) in July 2016.

THE POLICY

During G&P's time owning the Property, Deutsche Bank sued G&P seeking a declaratory judgment that its Deed of Trust survived the HOA's foreclosure. G&P ultimately prevailed in this lawsuit, with the court finding that the HOA's assessment lien had extinguished Deutsche Bank's interest in the Property due to Nevada statute NRS 116.3116, the terms of which designate HOA assessment liens as "super-priority" liens that are treated as senior to a first Deed of Trust. This provision also further provides that when such an assessment lien is foreclosed upon – as the HOA had done – the foreclosure operates to completely extinguish a Deed of Trust if one is present.

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[1] No. 84161, 2023 Nev. LEXIS 40 (Oct. 12, 2023).

While this suit was ongoing, Deutsche Bank submitted a claim for defense and indemnification under the Policy, which contained the following two ALTA/CLTA endorsements: (1) the first, CLTA 115.2(2), insured losses sustained "by reason of . . . [t]he priority of any lien for charges and assessments at Date of Policy in favor of any [HOA] . . . over the lien of [the] insured mortgage," and (2) the second, CLTA 100(1)(a), provided coverage for any losses sustained "by reason of . . . [t]he existence of any . . . covenants, conditions, and restrictions under which the lien of the mortgage . . . can be cut off, subordinated, or otherwise impaired" (both provisions collectively referenced as "the ALTA Endorsements").

The Policy also included CLTA 100(2)(a), which covered any losses sustained "by reason of . . . [a]ny future violations on the land of any covenants, conditions, and restrictions occurring prior to acquisition of title to the estate or interest . . . by the insured, provided such violations result in impairment or loss of the lien of the mortgage . . . , or result in impairment or loss of the title to the estate or interest . . . if the insured shall acquire such title in satisfaction of the indebtedness secured by the insured mortgage."

Additionally present in the Policy was a disclaimer providing that the endorsements contained therein were "made a part of the policy" and were "subject to all of the terms and provisions thereof and of any prior endorsements thereto," and a disclaimer stating that the endorsements "neither modif[y] any of the terms and provisions of the policy, nor . . . extend the effective date of the policy and any prior endorsements, nor . . . increase the face amount thereof."

THE CLAIM DENIAL

Ultimately, Fidelity denied Deutsche Bank's claim on the basis that the HOA lien did not come into existence and was not recorded until more than seven years after the Policy had been issued. As the recordation of this lien operated to terminate Deutsche Bank's interest, it followed that Deutsche Bank did not lose its interest until after the Policy date, and the claim thus fell within the Policy's exclusions.

Additionally, Fidelity determined that neither of the ALTA Endorsements provided coverage because it was not an *HOA* covenant, condition, or restriction that had caused the HOA's assessment lien to take priority over Deutsche Bank's lien, but rather the operation of Nevada's statute NRS 116.3116.

THE LOWER COURT LAWSUIT

Deutsche Bank later brought suit against Fidelity contesting the coverage denial, alleging numerous claims including breach of contract and breach of the

covenant of good faith and fair dealing. As its basis for these claims, Deutsche Bank contended that NRS 116.3116 should be treated as having been implicitly incorporated into the HOA's covenants, conditions, and restrictions, due to the NRS 116.3116 statute having been created in 1991, while the HOA's terms were declared in 2000. Deutsche Bank also produced title insurance trade manuals wherein Fidelity and other insurers had issued preliminary opinions stating they believed the ALTA Endorsements would potentially cover losses caused by super-priority HOA assessment liens.

Fidelity moved to dismiss on the same basis as its claim denial, with the lower court agreeing and dismissing Deutsche Bank's claims. In doing so, the lower court held that no coverage was owed under the Policy because the HOA assessment lien did not come into creation until the Lutkins became delinquent in 2011, and thus the lien constituted a post-policy lien outside the Policy's scope of coverage. As to Fidelity's contentions regarding the incorporation of NRS 116.3116, the court held that this allegation was irrelevant, as the assessment lien could only come into existence if a homeowner failed to timely pay an assessment.

The lower court also concluded that neither of the ALTA Endorsements afforded coverage, holding that CLTA 115.2(2) only covered losses suffered due to a lien existing or arising as of the date of the involved title policy – in this case May 2004 – and was thus not applicable in this matter as the assessment lien arose in 2011. As to CLTA 100(1)(a), the lower court held that because the endorsement did not expressly mention HOA assessment liens, it therefore did not cover losses from such liens, and further, that even if it potentially did, such protections would still not apply, as Deutsche Bank's losses were caused by NRS 116.3116 and not an HOA covenant, condition, or restriction. Finally, the lower court also held that CLTA 100(2)(a) was inapplicable, as the Lutkins' failure to pay the assessments owed was not a "violation on the land." In reaching these holdings, the lower court also rejected Deutsche Bank's trade usage evidence – the trade manuals and preliminary opinions – on the basis that they conveyed nothing more than uncommunicated, subjective intent that contradicted the Policy, which was an unambiguous contract.

THE APPEAL

Deutsche Bank later appealed the dismissal before the Court, with the Court affirming the dismissal as correct. In affirming, the Court began with the non-applicability of CLTA 115.2(2), noting that under NRS 116.3116, an assessment lien does not come into existence until a missing assessment payment actually becomes due. As the lien does not exist until such time, it follows that it cannot obtain its super-priority status at any time prior to its coming into existence. The Court thus held that in this case, both these events

– the arising/creation of the lien and it taking priority over the Deed of Trust via super-majority – occurred multiple years after the Policy date, thereby invalidating any claim for coverage.

Specifically, the Court held that "the applicability of CLTA 115.2(2) depends firstly on the existence of an assessment lien at the date of policy" and "depends secondly on whether that assessment lien, if in existence at the date of policy, has priority over the insured's mortgage under NRS 116.3116." In this instance, as the "assessment lien that ultimately extinguished Deutsche Bank's [D]eed of [T]rust did not exist until roughly seven years after the date of the [P]olicy . . . those losses [did] not fall within the scope of CLTA 115.2(2)." The same was true regarding priority, as the HOA's assessment lien only attained super-priority status "when the lien arose in 2011," and thus, the lien's priority displacing the Deed of Trust "arose roughly seven years after the [P]olicy date." Accordingly, the Court held that "there [was] no coverage for Deutsche Bank under CLTA 115.2(2)."

Turning to CLTA 100(1)(a), the Court held that for this endorsement to be triggered it was necessary for some aspect of an HOA covenant, condition, or restriction to have cut off, subordinated, or impaired the subject interest. In this instance – as Fidelity had consistently argued – it was not an HOA term, but instead NRS 116.3116, that provided for both the subordination and ultimate destruction of the Deed of Trust. Accordingly, there was no coverage under CLTA 100(1)(a).

Similarly, as to CLTA 100(2)(a), the Court observed that the "applicability of this endorsement presupposes that the losses resulted from a future violation of a" covenant, condition, or restriction, however, Deutsche Bank's losses in this instance resulted "because NRS 116.3116 created a statutory lien . . . comprised of a super[-]priority portion that, when foreclosed on, extinguishe[d]" Deutsche Bank's interest. Without "this statute, the failure to pay the assessment obligations, even if resulting in an assessment lien by virtue of the" covenants, conditions, and restrictions "would not extinguish" Deutsche Bank's interests. Therefore, "the losses arose by reason of NRS 116.3116," and because of this, no coverage was owed under CLTA 100(2)(a).

Therefore, based upon the above holdings, the Court affirmed the lower court's dismissal.

TAKEAWAYS

This opinion provides important guidance on the manner in which courts will interpret and apply the language of ALTA/CLTA endorsements 100(1)(a), 100(2)(a), and 115.2(2).

First, as to 100(1)(a), for coverage to be triggered it must be the precise covenant, condition, or restriction *itself* that results in the infringement of an

interest. If there exists interplay with a statute or other outside authority, for a claim to be viable, there must be certainty that ultimate responsibility for the infringement does not rest with the outside authority.

Similarly, under 100(2)(a), no coverage will be owed unless the ultimate cause of the complained of loss is a covenant, condition, or restriction.

Finally, as to 115.2(2), coverage will only be triggered where both: (1) the lien in question was actually in existence prior to or as of the date of the policy, and (2) that same lien also impacted priority as of the date of the policy or earlier.

Florida Appellate Court Holds Bank Does Not Owe a Duty to Refrain from Negligent Lending

The Florida Third District Court of Appeal (the Court) issued its opinion in the matter of *Suzmar v. First National Bank of South Miami*,[2] affirming the dismissal of a negligence claim brought against a bank on the basis that the bank had breached an alleged duty to refrain from negligent lending.

BACKGROUND

The matter arose out of a dispute between First National Bank of South Miami (First National) and Suzanne DeWitt (DeWitt), who claimed to be the manager and owner of a group of entities consisting of Plaintiff Suzmar, LLC and 16 other associated corporations (the LLCs). Based on DeWitt's ownership representations, First National issued her a $5.5 million dollar loan, with DeWitt using the LLCs as security for the loan. However, DeWitt's ownership claims were subsequently disputed by the Belgian corporation Agorive NV and found to be false, which caused First National to declare the loan in default. DeWitt was unable to return the full value of the loan funds or personally cover the shortfall, leading First National to assess the LLCs' various accounts for repayment.

The LLCs subsequently brought suit against First National for negligence and unjust enrichment, based upon the contention that First National had "improvidently grant[ed] the loan" to DeWitt. More specifically, they claimed that First National had failed to adequately investigate DeWitt prior to issuing the loan, with the LLCs describing DeWitt as "a Miami attorney who claimed to own the LLCs, and used their accounts as collateral [and] security[,] despite inconsistencies in her loan application." The LLCs contended that this alleged

[2] No. 3D22-1839, LEXIS 6065 (Dist. Ct. App. Aug. 30, 2023).

inadequate investigation of DeWitt constituted a violation of the "know-your-customer" requirements imposed by the Bank Secrecy Act.[3]

In response, First National moved to dismiss these claims, asserting that the LLCs were unable to state a valid cause of action because: (1) Florida law does not recognize a claim for negligent lending absent a fiduciary relationship, and (2) a claim for unjust enrichment cannot lie without a windfall benefit. The trial court granted this motion to dismiss, leading the LLCs to appeal the dismissal before the Court.

THE APPEAL

In addressing the appeal, the Court began with the LLCs' negligence claim, which it observed was premised upon the allegation that First National had owed the LLCs a duty to act in good faith. This duty was allegedly breached when First National failed to comply with the "know-your-customer" requirements and issued the loan to DeWitt despite her having made false representations in support of her application. The Court next noted that to successfully state a negligence claim, it is incumbent upon the plaintiff to establish the existence of a legally recognized duty – however, citing Florida case law, the Court held that "banks have no duty to customers to prevent negligent lending absent a fiduciary relationship."

The Court then proceeded to find that no fiduciary relationship existed between First National and the LLCs, as the Florida general rule holds that the relationship between a bank and its borrowers is "that of a creditor-debtor" and, accordingly, a "bank does not owe a borrower a fiduciary duty." Thus, the Court affirmed that the trial court had properly dismissed the negligence claim against First National, as absent the existence of a fiduciary relationship between the parties, First National did "not owe the LLCs a duty to refrain from negligent lending." Additionally, the Court held that the "know-your-customer" requirements relied upon by the LLCs could not create or impose a duty upon First National, as based upon Eleventh Circuit precedent, bank consumers "do not have a private right of action to enforce these rules."

As to the LLCs' remaining unjust enrichment claim, the Court held that it was "similarly insufficient," as unjust enrichment cannot exist where payment

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[3] The "know-your-customer" requirements of the Bank Secrecy Act – found at 31 31 U.S.C. § 5318 – impose a set of guidelines to which financial institutions and businesses are required to adhere in order to prevent money laundering and other financial improprieties, requiring that a lender verify the identity, suitability, and risks of all current or potential customers. The goal of these obligations is to preemptively identify suspicious behavior such as money laundering or financial terrorism.

or other adequate consideration has been made for a benefit conferred. Accordingly, the Court held that the LLCs had failed to state a sufficient cause of action for unjust enrichment, as the loan to DeWitt "was adequate consideration to someone related to the LLCs for the benefit conferred."

Therefore, based upon the above, the Court affirmed the trial court's dismissal of the LLCs' claims.

TAKEAWAYS

This opinion demonstrates that absent an additional agreement voluntarily entered into between the parties, a bank will not owe its consumers a fiduciary duty, nor will such a duty be imposed despite a bank having clearly erred. It also demonstrates that even where a violation of the Bank Secrecy Act has seemingly occurred, an action for this violation will only be permissible if brought by the proper officials possessing enforcement authority under the statute.